United States Court of Appeals

for the Second Circuit

REPLY BRIEF

74-2081

To be argued by
I. STEPHEN RABIN

B
P/S

United States Court of Appeals

For the Second Circuit

ROBERT L. SCHWARTZ, RICHARD F. KNAPP, RUDOLPH J. MUELLER, LAWRENCE F. McGIVNEY, SIDNEY J. HELLER, GARBIS G. TAKESSIAN, NORBERT W. DOYLE, STANLEY F. POPEIL, WILLIAM E. LANGE, E. LEE MULLER, ROBERT E. McDONNELL, III and JOHN F. SWAN,

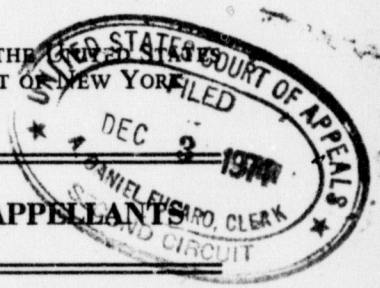
Plaintiffs-Appellants,

—against—

McDONNELL & CO., INCORPORATED, T. MURRAY McDONNEL, MORGAN McDONNELL, EDWARD F. BECKER, FRANK V. DEEGAN, WILLIAM J. CORBETT, RAYMOND J. DOYLE, JR., HUBERT McDONNELL, JR., JOHN J. DELLASSANDRO II, and NEW YORK STOCK EXCHANGE, INC.,

Defendants-Appellees.

ON APPEAL FROM A JUDGMENT AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK
(71 Civ. 1281)



REPLY BRIEF FOR PLAINTIFFS-APPELLANTS

RABIN & SILVERMAN
Attorneys for Plaintiffs-Appellants
80 Broad Street
New York, New York 10004
212-248-6490

Of Counsel:
I. STEPHEN RABIN

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REPLY BRIEF FOR PLAINTIFFS-APPELLANTS

There are several incorrect statements of "fact" made by defendants that, at the outset, should be corrected:

1. The plaintiffs did not, at any time, neglect the prosecution of this case. They relied upon a discovery stipulation that is binding on the Exchange and McDonnell (35a) as they had every right to, and by agreement with Davis & Cox that firm took the laboring oar as to discovery. One reason why this case has not already been tried is that the Exchange took five months to comply with a request for documents that should have been complied with in thirty days. (40a; 67a; 130a).

2. There is no "mystery" concerning the identity of Donald M. Kresge. He was an associate professor of law at Ohio Northern University from September, 1973 to July, 1974 (177a). No formal substitution of counsel was filed because certain matters relating to the payment of defendants' counsel fees remained unresolved (*cf.* plaintiff's brief, p. 6). The opinion of the District Judge lists and refers to Frank Greenberg of Rabin & Silverman as plaintiffs' attorney (236a; 238a-239a), which clearly shows that there was no confusion as to who was in charge of the litigation for the plaintiffs.

3. As will be discussed below, between the November 21, 1973 Magistrate's meeting and the meeting held on May 17, 1974, Davis & Cox deposed the Chief Examiner of the Exchange (three deposition sessions); the partner at Coopers & Lybrand, auditors for McDonnell, who was in charge of the McDonnell account (four deposition sessions); and ~~Murray~~ McDonnell, a member of the Senior Management Board of McDonnell and a defendant herein. All of these depositions added materially to the body of evidence available to plaintiffs. Thus, by virtue of the discovery stipulation plaintiffs could state by May 17, 1974 that they had no need for further discovery. This conclusion of plaintiffs was not "conjured up."

POINT I

The discovery conducted by the Davis & Cox firm is usable in this case, plaintiffs were prepared to go to trial, and the District Court abused its discretion in dismissing this case.

In view of the stance of the defendants—that the discovery taken in the two cases being prosecuted by the firm of Davis & Cox is not usable in this case, it is appropriate to refer this Court to the two complaints in those actions in

order to show that on many issues those actions overlap with this one.*

Briefly put, in the first of the two actions being prosecuted by Davis & Cox, *Margaret Mary McDonnell Murphy* v. *McDonnell & Co., Incorporated, et al.*, 71 Civ. 461, the complaint alleges that, among other things, in late 1968 and early 1969 McDonnell was financially so weak it could not comply with the net capital rules of the Exchange, and the Exchange knew this but allowed McDonnell to continue doing business with the public without the disclosure of its parlous condition. The *Murphy* complaint goes on to allege that McDonnell took advantage of this induced secrecy as to its condition, and in January and February of 1969 fraudulently induced the plaintiff Murphy to enter into a subordinated loan agreement with McDonnell. It alleges that the Exchange knew or should have known of the true condition of McDonnell, and approved the subordinated loan without requiring that Murphy be informed of McDonnell's true condition (R 20).

The second of the two suits being prosecuted by Davis & Cox is *Anna M. McDonnell, et al.* v. *The New York Stock Exchange, et al.*, 71 Civ. 1940. The complaint in that action contains the same allegations as to McDonnell and the Exchange as are contained in the *Murphy* complaint—that McDonnell was skirting financial disaster in late 1968 and early 1969, and that the Exchange knew or should have known of this condition and of McDonnell's breach of the Exchange's net capital rules. This second suit concerns the sale to one plaintiff of a McDonnell debenture without disclosure of McDonnell's financial condition, and other

* The complaints in both *Margaret Mary McDonnell Murphy* v. *McDonnell & Co., Incorporated, et al.*, 71 Civ. 461, and *Anna M. McDonnell, et al.* v. *The New York Stock Exchange, et al.*, 71 Civ. 1940, are made a part of the District Court record herein at R 20.

transactions by McDonnell, with other plaintiffs, without proper financial disclosure.

Thus, there are issues of law and fact common to all three actions. The complaint in the present action, like the complaints in the two Davis & Cox litigations, alleges that McDonnell's financial condition in late 1968 and early 1969 was misrepresented; that the Exchange knew, or should have known, of McDonnell's true condition; and that the Exchange did not fulfill its duties under the Securities Exchange Act of 1934 and its own rules to regulate McDonnell, including the regulation of McDonnell's capital raising activities (1a-32a).

From the foregoing it will be seen that while the plaintiffs in the present action had good reason to resist a motion made by the Exchange to consolidate this case with the two Davis & Cox cases (R 20), the stipulation requiring the coordination of discovery that was entered into among the Exchange, McDonnell, and the plaintiffs in all three actions was an eminently sensible way to avoid duplication of discovery.*

The discovery stipulation, entered into on July 22, 1971 (36a), to which the Exchange and McDonnell are parties, states the notices of depositions, in any of the three actions, shall be served on all parties to the stipulation, and that depositions so noticed

> "shall be deemed to be taken in all of said actions and may be used in each of said actions for the same

* Parenthetically, it should be noted that contrary to the assertions of the District Court (243a fn. 1) and the defendants (brief p. 7 fn.), the consolidation motion was never "successfully opposed" by plaintiffs. As the stipulation makes clear, it was withdrawn without prejudice by the Exchange (35a-36a). This misstatement of fact is typical of the numerous incorrect assumptions upon which the District Court's opinion is based, and is another instance of that Court being misled by the defendants.

purpose and to the same extent as if taken in such action." (36a)

Thus, the contention of the defendants, at this late date, that the depositions are not fully usable against the Exchange and McDonnell, dishonors an agreement these parties made over three years ago. As could be expected, the plaintiffs relied on the stipulation and made it the cornerstone of their discovery strategy. (Of course, the Exchange and McDonnell had notice of all of the foregoing Davis & Cox depositions.)

As noted in plaintiffs' main brief at 20-21, the depositions could be used against the Exchange and McDonnell under any reading of Rule 32. And as noted in plaintiffs' main brief at 19-21, under the prevailing liberal construction given to Rule 32, the depositions should be usable for impeachment purposes, and additional purposes other than for their truth, against the other defendants in this action. For although the two Davis & Cox litigations are being prosecuted separately, the subject matter of the depositions relates to issues identical to issues herein.

Likewise, under the stipulation the documents produced by the Exchange and McDonnell in the Davis & Cox litigations, including the documents produced pursuant to the order of July 21, 1974 (*see* plaintiffs' brief at 5) are deemed produced in this action and are available to plaintiffs (36a).

It is also appropriate to take note of the extent of the discovery that has been conducted by Davis & Cox in the two related cases it is prosecuting. The following table

sets forth some of the persons deposed by Davis & Cox, including the dates on which deposition sessions were held and the total pages of transcript in each deposition:

Name	Position	Deposition Dates	Total Pages in Deposition Transcript
Individual Defendants Herein			
T. Murray McDonnell	Chief Executive Officer of McDonnell	6-28-73 7-9-73 7-12-73 7-30-73	376
Morgan McDonnell	Member, Senior Management Board of McDonnell	1-4-74	118
Representatives of the Exchange			
Robert M. Bishop	Senior Vice President in charge of Dept. of Member Firms	4-24-73 4-25-73 4-30-73 5-1-73	494
Lloyd McChesney	Chief Examiner	1-11-74 1-21-74 1-22-74	315
Lee D. Arning	Vice President and Operations Officer	6-7-73 6-8-73 6-19-73	327
Andrew R. McElroy	Supervising Senior Examiner, Dept. of Member Firms	6-6-73	146
Herbert E. Schuette	Coordinator, Division of Supervisory Standards	6-21-73	208
Fred J. Stock, Jr.	Vice President and Associate Director, Department of Member Firms	6-12-73	209
Robert A. Spies	Finance Specialist, Division of Finance	5-31-73	140
David Fuchs	Assistant Director, Cost Revenue Division	6-14-73	54

Name	Position	Deposition Dates	Total Pages in Deposition Transcript
William G. Carr	Manager, Division of Documents	7-5-73	146
W. Ellsworth Jones	In Charge, Division of Finance and Division of Documents	6-27-73	98
Richard A. Grieves	Assistant Coordinator and Coordinator	6-5-73	65
Paul H. Fitzgerald	Supervisor, Division of Member Offices and Personnel	6-15-73	100
George H. Newman	Manager of Division of Finance	5-10-73	300
Other Persons			
Alvin J. Mentzel	Partner, Coopers & Lybrand, Auditors for McDonnell	1-29-74 2-12-74 2-13-74 2-21-74	372
Richard Olney III	Vice President of McDonnell	7-10-73	151
Thomas P. Ford	Partner, Shearman & Sterling, Attorneys for McDonnell, in charge of McDonnell Account	10-3-73	101
David W. Rome	Controller of McDonnell	9-25-73	158

POINT II

The District Court evaluated the substance of plaintiffs' evidence without having the evidence before it, contrary to procedures prescribed in the Federal Rules and contrary to due process of law.

A further word is in order about the assertion of the defendants that the Davis & Cox discovery and the stipulation were of no value to the plaintiffs.

There is no requirement, under the Federal Rules or elsewhere, that the plaintiffs had to conduct a given quantum of discovery before they could decide that they were ready for trial. If plaintiffs were wrong in their decision, the decision could have been tested by means provided in the Federal Rules. Defendants could have moved for summary judgment under Rule 56, or after plaintiffs put in their case at the trial, moved for a directed verdict under Rule 50.

The procedure followed here by the District Judge, however, in evaluating the substance of plaintiffs' evidence, including the over 3,200 documents plaintiffs *themselves* obtained under Rule 34 (40a-66a), disregards these prescribed methods for testing plaintiffs' case.

When the District Judge determined that plaintiffs had not conducted enough discovery and therefore kept them from going to trial, he made the determination without having before him the contents of the documents obtained through discovery, the arbitration and deposition transcripts, and the documents turned over to the plaintiffs by the Securities and Exchange Commission. These documents had *never* been before him, or before the Magistrate. The procedure followed by the District Judge not only has no basis in the Rules, it was an evaluation of a party's proof without a hearing on that proof, and a denial of "those fundamental requirements of fairness which are the essence of the process in a proceeding of a judicial nature." *Morgan* v. *United States*, 304 U.S. 1, 19 (1938). It therefore was a denial of the due process of law guaranteed by the Fifth Amendment. Ibid.

POINT III

Defendants' authorities do not support dismissal when plaintiffs are ready to go to trial but defendants have conducted no discovery whatsoever.

As discussed in plaintiffs' main brief, the decision of the District Judge was contrary to the controlling law in this

and other Circuits. The cases relied upon by defendants do not demonstrate that, when a plaintiff is fully prepared to go to trial, and his adversaries have yet to conduct their discovery, the plaintiffs' case may be dismissed for lack of prosecution.

Thus, in *West* v. *Gilbert*, 361 F. 2d 314 (2d Cir.), cert. denied, 385 U.S. 919 (1966), the plaintiffs noticed a deposition on August 14, 1964 when they were under a pre-trial order to file a note of issue by August 17, 1964. The order expressly stated the case would be dismissed if the order was not complied with.

In *Theilman* v. *Rutland Hospital, Inc.*, 455 F. 2d 853 (2d Cir. 1972), the plaintiff's attorney was not prepared to go to trial after the jury had already been sworn. This Court particularly emphasized the waste of a jury that resulted from the attorney's conduct. Id. at 856.

In *Theodoropoulos* v. *Thompson-Starrett Co., Inc.*, 418 F. 2d 350 (2d Cir. 1969), cert. denied, 398 U.S. 905 (1970), plaintiffs' discovery likewise was not completed by the expiration of a deadline set in a pretrial order.

CONCLUSION

The dismissal should be vacated and the plaintiffs should be permitted to have a trial on the merits.

Respectfully submited,

RABIN & SILVERMAN
Attorneys for Plaintiffs-Appellants
80 Broad Street
New York, New York 10004

I. STEPHEN RABIN
of Counsel

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

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On Appeal From a Judgment and Order of The United States District Court for The Southern District of New York (71 Civ. 1281)

STATE OF NEW YORK)
) SS:
COUNTY OF NEW YORK)

LOUIS MARK, being duly sworn, deposes and says: That he is over twenty-one years of age: That on the 3rd day of December 1974 he served two copies of the attached Reply Brief for Plaintiffs-Appellants on each of the following named by enclosing said copies in fully post-paid wrappers addressed as follows and depositing same in The United States Post Office maintained at No. 150 Christopher Street, New York City, New York.

Milbank Tweed Hadley & McCloy, Esqs.
One Chase Manhattan Plaza
New York, New York 10005

Proskauer Rose Goetz & Mendelsohn, Esqs.
300 Park Avenue
New York, New York 10017

Lunney & Crocco, Esqs.
20 Exchange Place
New York, New York 10005

Reavis & McGrath, Esqs.
One Chase Manhattan Plaza
New York, New York 10005

Burns Kennedy Shilling & O'Shea, Esqs.
598 Madison Avenue
New York, New York 10022

Louis Mark

Sworn to before me this
3rd day of December 1974

Quinton C. Van Wynen

QUINTON C. VAN WYNEN
Notary Public, State of New York
No. 24-4087465
Qualified in Kings County
Commission Expires March 30, 197[illegible]

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